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Supreme Court, U.S.
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IN THE

Supreme Court of the United States

THE WHARF (HOLDINGS) LIMITED, a Hong Kong company; WHARF COMMUNICATIONS INVESTMENTS LIMITED, a Hong Kong company; AND STEPHEN NG, a Hong Kong citizen,

Petitioners,

v.

UNITED INTERNATIONAL HOLDINGS, INC., a Delaware corporation; AND UIH ASIA INVESTMENT CO., a Colorado general partnership,

Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit

BRIEF FOR RESPONDENTS

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QUESTIONS PRESENTED

By Order, filed November 6, 2000, this Court granted certiorari in respect of the following questions:

1. Whether the Court of Appeals erred in holding that Section 10(b) of the Securities Exchange Act of 1934 and SEC Rule 10b-5 apply to disputes over the ownership of securities where there is no claim that financial information was misrepresented or not disclosed?

2. Whether the Court of Appeals erred in holding that Section 10(b) and Rule 10b-5 apply where plaintiffs' only claim seeks damages for nonperformance of an alleged unenforceable oral option?

The Court did not grant certiorari on three other questions Wharf presented, which concerned choice of law, the exercise of supplemental jurisdiction over the state law claims, and the calculation and award of damages.

RULE 29.6 STATEMENT

Respondent United International Holdings, Inc. ("UIH"), now called UnitedGlobalcom, Inc., is a publicly held company with no other parent. Liberty Media Corporation owns more than ten percent of the stock of UnitedGlobalcom, considering all classes of stock together.

Respondent UIH Asia Investment Company is a general partnership with no other parent. UnitedGlobalcom owns 80 percent of the stock of UIH Asia Investment Company.

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THE WHARF (HOLDINGS) LIMITED, a Hong Kong company; WHARF COMMUNICATIONS INVESTMENTS LIMITED, a Hong Kong company; AND STEPHEN NG, a Hong Kong citizen,

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v.

UNITED INTERNATIONAL HOLDINGS, INC., a Delaware corporation; AND UIH ASIA INVESTMENT CO., a Colorado general partnership,

Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit

BRIEF FOR RESPONDENTS

STATUTES INVOLVED

In addition to the statutes provided by petitioners, 28 U.S.C. §§ 1331 and 1367 are set forth in an attached appendix to this brief.

STATEMENT

Respondents (collectively, "UIH") show in this brief that the Court should affirm the Tenth Circuit's decision for two distinct reasons. First, UIH pled, proved, and won a valid SEC Rule 10b-5 claim; all of petitioners' (collectively, "Wharf's") arguments depend on ignoring (or relitigating in this Court) the facts found by the jury. Second, since the

district court plainly had jurisdiction under 28 U.S.C. §§ 1331 and 1367, and Wharf does not seriously challenge the jury verdicts holding it liable for fraud and for breach of fiduciary duty to a joint venture partner under Colorado law and awarding the full amount of damages on each count, the judgment below does not depend on the answers to the Rule 10b-5 questions on which this Court granted certiorari.

UIH pled and proved, and the jury found in a detailed special verdict, a black-letter violation of SEC Rule 10b-5, 17 C.F.R. § 240.10b-5. *See* J.A. EP-7, 11-13.[1] At an October 8, 1992 meeting in Denver, Wharf sold UIH an option (the "Option") to purchase 10% of the stock of a company called CNCL, whose subsidiary, Wharf Cable, was bidding for the exclusive franchise to provide cable TV service in Hong Kong.[2] The Option was a "security" as defined in section 3(a)(10) of the Securities Exchange Act of 1934 ("Exchange Act"), 15 U.S.C. § 78c(a)(10). The agreed purchase price of the Option was substantial services to be rendered by UIH. UIH promptly paid that price, assigning certain of its senior personnel, at its own expense, to fill key positions at Wharf Cable and providing other services Wharf requested. In connection with the sale, Wharf deliberately and materially deceived UIH: As UIH proved at trial with evidence including documents from Wharf's own files, Wharf never had any intention of allowing UIH to exercise the Option.

Wharf's violation of Rule 10b-5 was part of a two-year fraudulent scheme. Wharf urgently needed UIH as a "strategic partner" (Wharf's term) to win the franchise and design and build the cable system. By promising and then

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[1] Citations to the Joint Appendix are in this format. Citations to the Lodging to the Joint Appendix are to "L.J.A._____." Citations to Appellants' Appendix in the Court of Appeals are to "Aplt. App.___."

[2] L.J.A. DP shows the relationship of CNCL to petitioners when the Option was sold.

selling UIH a worthless security, Wharf obtained the benefit of UIH's name, reputation, industry connections, expertise, and managerial help and won the franchise. Wharf strung UIH along until Wharf felt it no longer needed UIH and then, as it had planned all along, refused to allow UIH to exercise the Option. UIH alleged and proved, and the jury found in separate special verdicts, that in addition to violating Rule 10b-5, Wharf had also violated the Colorado Securities Act and committed common law fraud, breach of fiduciary duty to a joint venture partner, breach of contract, and negligent misrepresentation under Colorado law. *See* J.A. EP-1-11.[3]

The jury instructions (J.A. EM-1-83) defining these several claims and the measure of damages for each claim were essentially agreed and not challenged on appeal. The jury awarded UIH $67 million in compensatory damages separately on each claim (except negligent misrepresentation, on which it awarded $8.1 million). *See* J.A. EP-1-13. After finding "beyond a reasonable doubt" that Wharf's actions were "attended by circumstances of fraud, malice, or willful and wanton conduct," the jury awarded $58.5 million in exemplary damages on both the fraud and breach of fiduciary duty claims. *See* J.A. EP-4-5, EP-11. Because UIH was entitled to only one recovery, the district court added $67 million and $58.5 million and entered judgment for $125.5 million. *See* Pet. App. E-1-4. The court of appeals affirmed, rejecting each of Wharf's federal and state law arguments, often on multiple grounds. *See* Pet. App. B-1-46.

A. Proceedings in the District Court.

Wharf's Statement all but ignores the facts that UIH pled and the jury found after an 11-week, 39-witness, 1600-

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[3] The jury also found that defendants Wharf Holdings and Wharf Communications were liable as "controlling persons" under Section 20(a) of the Exchange Act, 15 U.S.C. § 78t(a). *See* J.A. EP-35-39.

document trial.[4] UIH pled and proved that Wharf sold UIH a security, the Option, on October 8, 1992; that UIH provided indispensable services to Wharf in return; and that Wharf deliberately and materially deceived UIH in connection with the sale. Wharf contended at trial that the sale did not occur, and that UIH provided its concededly extensive services as a volunteer, merely hoping for an investment opportunity, but the jury rejected Wharf's contentions. The court of appeals found "ample evidence in the record to support the jury's finding that UIH obtained an option on October 8, 1992." Pet. App. B-28. Wharf is not entitled to ignore UIH's Complaint or relitigate the facts in this Court.

1. UIH's Complaint.

The Option was not, as Wharf improperly suggests (Brief for Petitioner ("Br.") 21), a "judicially fashion[ed]" afterthought of the Tenth Circuit. UIH's Complaint pled in detail the existence, terms, and fraudulent sale of the Option. *See* J.A. F-1-2, 5-19, 22-24. It alleged that on October 8, 1992, at UIH's offices in Denver, petitioner Stephen Ng, Wharf's Managing Director, "confirmed an agreement" that "[UIH] had the option . . . to purchase . . . 10% of the capital stock of CNCL." J.A. F-13-14. It alleged that the price of the Option was UIH's assistance to Wharf in obtaining the cable franchise. *See* J.A. F-15. It set forth the Option's terms: the exercise price would be 10% of the equity capital needed for the project; the Option would expire if not exercised within six months after the franchise award; and in order to exercise, UIH would need to demonstrate its ability to fund 18 months of its share of the projected equity requirements. *See* J.A. F-14-15. It alleged that "[t]he grant of the option . . . was the sale of a security to [UIH] within the meaning of the Securities Exchange Act" (J.A. F-22), and that Wharf defrauded UIH in connection with the sale: "[A]t

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[4] Before trial, the district court denied Wharf's motions for summary judgment. *See* 946 F. Supp. 861 (D. Colo. 1996).

the time [UIH] was granted the option, [Wharf], through Ng, represented that [UIH] would be entitled to exercise the option . . . . These representations were false when made . . . ." J.A. F-22-23. It alleged that Wharf acted with scienter (*see* J.A. F-23), that the representations were "material" (*id.*), and that UIH "reasonabl[y] and justifiably relied" on them and incurred damage as a result (*see* J.A. F-24). In addition to the Rule 10b-5 and "controlling person" claims (*see* J.A. F-24-25), UIH alleged that Wharf's conduct over more than two years violated the Colorado Securities Act and constituted fraud, breach of fiduciary duty, breach of contract, and negligent misrepresentation. *See* J.A. F-1-20, 25-30; *see also* J.A. I-3-5 (Pretrial Order).

2. The Proof at Trial.

At trial, UIH proved the following facts:

In 1991, Hong Kong was one of the largest undeveloped cable TV markets in the world, and the Hong Kong Broadcast Authority ("BA") was expected to announce competitive bidding for an exclusive franchise. *See* J.A. DK-16-19; BM-1-5. Wharf was determined to bid, but its only cable TV experience was forming a consortium in the 1980s that quickly collapsed. *See* J.A. CE; DK-16-19, 29-39. Wharf recognized that to prepare its bid, make itself credible to the BA, and design and implement its system, it needed "one or two major partners" with "experience," "technical expertise," and "credibility," (J.A. DK-39-61; DT-29-39; L.J.A. A-3, 8-9; B-1, 4, 6, 11; C-1; U-9-10, 22-23), ideally including a Denver cable TV company (*see* J.A. DK-49-50; L.J.A. K-1).

Wharf chose Denver-based UIH as its "strategic partner" (*see* J.A. K-14-16; W; X-2-3; Z; DB-1-4; L.J.A. AC-22; AA-3; BD-2; BF; BK; BQ; CD), and the choice was appropriate. UIH's founders had a long history in the cable TV business. *See* J.A. K-1-8; DD; Y-1-9. In 1992, UIH had ownership interests in cable TV businesses in six countries. *See* L.J.A. AB-6; BA-39. As Wharf recognized, "UIH combines U.S.

. . . and international cable expertise," and is a "leader[] in the . . . world, [in cable TV]." L.J.A. AE-3; U-9-10. Petitioner Ng, acting for Wharf, asked UIH to be Wharf's "strategic partner" and "help [Wharf] develop [its] expertise and build [its] business plan, win [the] bid, and help implement the business." J.A. X-2; W-21-24; Z; DK-11; *see also* L.J.A. N-1.[5]

Importantly, UIH was not a consulting company (*see* J.A. DI-10-15; K-13-23; AA-1-6; W-1-2; BM-2-5; DT-46-47 (Ng)), and it made clear from the outset that it would work with Wharf only as "part of an ownership group" (J.A. W-9; BM-9-10; DG). Thus, from the beginning of their discussions in 1991, UIH and Wharf negotiated a relationship under which UIH would receive an option to purchase at least a 10% interest in the cable project. *See* J.A. W; BM; X; L.J.A. D; E; F; G; I; J; L. Both parties understood that Wharf would *not* pay UIH a fee or reimburse any of its costs. *See* J.A. DB-1-3; Z-6-9; P-3-4. On the contrary, UIH began to assist Wharf in the summer of 1992 because Ng offered UIH the right to invest at "a 10% level" as a partner in the business (J.A. X-2; *see also* J.A. Z; L.J.A. P-1-5) and said that UIH's rights would be reflected in Wharf's September 30, 1992 bid for the cable franchise.[6]

As filed on September 30, 1992, Wharf's bid package devoted over 30 single-spaced pages to describing UIH and its expected contributions as a "strategic partner." *See* L.J.A. BA-33-67. UIH allowed this use of its name and description

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[5] According to Wharf, "strategic partner" meant a firm that "will participate at a ground floor level alongside Wharf and share proratably in both the up side and down side of the venture." J.A. DT-51-52 (Ng); L.J.A. E (Ng tells UIH he envisages that partner to venture will contribute expertise and capital); *see also* J.A. W-13-15; AY-1-2; K-14-16; DI-1-6; BM-4 (testimony re common understanding of "strategic partner").

[6] *See* J.A. P-1-10; DB-5-6; AC; CI; BU; CQ-9-16; L.J.A. AZ; *see also* J.A. X-3-6; W-10-12; K-18-23; Y-5-6; BT; BH-1-9; L.J.A. AC-22-25; AE-2; T-17.

of its anticipated contributions because of Ng's promises and because Wharf's Emil Fung, Ng's deputy, showed UIH a draft of Wharf's bid (*see* L.J.A. AO-1) stating *to the Hong Kong Broadcast Authority* that Wharf had "*offered*" UIH an "*option*[]" to purchase 10% of the stock of CNCL. J.A. BO-1-30; L.J.A. AK-2; AL; AM; AN; AP; AR; AS (notes discussed in J.A. BO); J.A. AB 5-12; DB-5-13; DW-51-52; Pet. App. B-6. But without telling UIH, Wharf pulled this language out immediately before the bid was filed, shocking UIH and precipitating the sale of the Option.[7] *See* J.A. BO-31-36; P-7-11; AB-10-12.

After the bid was filed, Wharf needed immediate additional help. *See* J.A. P-13-17; DB-15-21; BP-1; BD-43-48. Wharf Managing Director Ng came to Denver and met on October 8, 1992 with UIH Chief Executive Officer William Elsner and President Mark Schneider at UIH's offices. *See* L.J.A. BB-2-3. At that meeting, as both Elsner and Schneider testified in detail (and as Ng essentially conceded except as to the sale of the Option), Ng asked UIH immediately to "second" key UIH personnel, at UIH's expense, to full-time senior management positions at Wharf Cable in Hong Kong. *See* J.A. AF-1-3; P-13-17; BO-36-37. Elsner and Schneider, surprised by Wharf's last-minute deletion from the bid of the statement that UIH had been "offered" an "option," told Ng that UIH would *not* help (and would inform the BA that UIH would have no further

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[7] Based on Wharf's representations (*see* J.A. BO; AB-6-9), UIH and Wharf Cable signed a Technical Cooperation Agreement ("TCA") on September 25, 1992, providing for certain assistance from UIH if and when (but only after) the franchise was awarded. J.A. CG. In an unchallenged instruction, the jury was told that the TCA with Wharf Cable did not bar UIH's claim that Wharf Cable's parent companies had sold UIH an option. *See* J.A. EM-51. As the Tenth Circuit noted (*see* Pet. App. B-5), the parties deleted an "integration clause" from the TCA to avoid any implication of eliminating UIH's investment rights. *See* L.J.A. AQ-14; J.A. B0-27-31; *see also* BO-5-6; AT-10-17; BN; DB-5-18; S; AE; DW-49; BD-27-42; L.J.A. EH.

dealings with the project) unless Wharf then and there granted the Option. *See* J.A. AF; AW; P-15-23; Pet. App. B-6.[8] Ng, acting for Wharf, granted UIH the Option in return for UIH's agreement to provide the requested personnel immediately and otherwise continue as Wharf's strategic partner. *See* J.A. P-12-23; AF-7-13; AT-1-8; U-2; AR-4-7; Pet. App. B-6. The parties intended the agreement to be binding and enforceable immediately, and to be documented later. *See* J.A. U; AF; AA-5-9; AH; DI-11-15; BO-41-45.

Immediately after the October 8 meeting, Ng, Elsner, and Schneider told other UIH personnel that agreement had been reached. *See* J.A. DB-22-28; BO-37-40; DH-1-3; CW-3-4. UIH promptly assigned three senior UIH employees to Wharf to help create the cable system and provided the other help that Ng had requested. *See* J.A. AR. Moreover, UIH personnel acted on what they were told in their dealings with third parties, who were told of UIH's rights. *See, e.g.*, J.A. V; BH-9-26; CT; L.J.A. BG-1; BP-18; CG-4; CR-17; CT; DA-8.

Wharf argued to the jury, as it does to this Court, that various unsigned documents supported its factual contention that it did not sell UIH an Option on October 8. At trial, each of the documents Wharf now invokes was the subject of extensive testimony and cross-examination that put them into proper context and refuted the same contentions that Wharf now makes. *See, e.g.*, J.A. BV; DY; CI; BK; BU; AB-1-5;

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[8] Wharf asserts in this Court that "Mr. Ng has consistently denied that any such conversation took place." Br. 12. That is untrue: Ng's testimony was neither consistent nor a denial of the conversation. *See, e.g.*, J.A. BD-43-57. Ng denied granting the Option, but it is not surprising that the jury believed Elsner and Schneider and not Ng. In Ng's video deposition, which was played to the jury, his response to hundreds of questions, including many about the October 8 meeting, was "I don't recall." *See, e.g.*, J.A. BD; BG; DV. At trial, he claimed to remember more, and suggested that returning to Denver had rejuvenated his memory. *See* J.A. DS-1-2. But he contradicted himself and was impeached with his deposition dozens of times. *See* J.A. DT.

CF. Witnesses explained that the pre-October 8 unsigned documents illustrate frustrations that led to the October 8 sale (*see, e.g.*, J.A. BK; CF; BU; BO; DB-6-13, 16-19), and that post-October 8 documents on which Wharf relies were, in general, the result of discussions regarding whether UIH could reach a new agreement to increase its 10% share to 20% (*see, e.g.*, J.A. AG; AV; AQ; AU; BQ; BL; BS; BR; EM-48; L.J.A. CS-1 (Wharf: UIH now asking for 15% in CNCL, but "10% . . . was the basis of our original understanding")), and efforts to document UIH's rights in the face of Wharf stalling tactics that were part of its fraud. *See, e.g.*, J.A. BO-41-45; AT-1-9; AV; BI; AQ; L.J.A. CH-1; J.A. BS; BR; L.J.A. CU-1; J.A. BA; AU; AY; AZ; AL; AM; AN; AO; AP.

Wharf also claimed at trial, as it does here, that UIH's right to exercise the Option was subject to certain unsatisfied Wharf conditions. UIH's witnesses testified emphatically that no such conditions existed. *See* J.A. AF-10-11; *see also* J.A. AB-1-5; P-21 (no board condition); AT-3-4; AF-8-10; P-22-23; U-2; BU; Z-9-14 (no NYNEX condition); U; AF-12; AG; AH (no documentation condition). Wharf's witnesses conceded that these conditions were imaginary. *See, e.g.*, J.A. CD-2 (Wharf officer concedes board approval not needed); J.A. DW-6-12; BD-89-90, 93-96, 99; CH-2 (Wharf witnesses concede Wharf never said NYNEX investment was condition to UIH investment); J.A. EA; EB-1-2; AI; AK (NYNEX unaware of any such condition).

UIH's assistance to Wharf was immense: UIH personnel helped Wharf prepare the project's business plan (*see* J.A. AR-8-10; P-2-3; Z-1-9; CQ-9-15; DB-1-4; L.J.A. AZ-1); served as the project's interim Chief Operating Officer, Chief Engineer, and in other managerial roles (*see* J.A. AR-20; CQ-1-8, 9-29; CJ-7-8; L.J.A. BJ-4; BH-1; BV-2); negotiated key supply contracts (using UIH's business relationships to obtain favorable pricing for Wharf) (*see* J.A. AR-10-13; CO; CR; DB-18-21; CZ; L.J.A. DO); helped

design and shape the project's technical and operational aspects (*see* J.A. DO; AR-14-15; CL-3-38; CQ; DC; Aplt. App. 5005-15; L.J.A. DO); identified and recruited most of the project's permanent senior operations managers (*see* J.A. AR-21; CK; CL-1-3; DB-15-17); and helped to obtain the project's debt financing (*see* J.A. AR-15-18; BH-14-27, 159-60). Wharf's internal documents noted, and Wharf's witnesses admitted, that UIH was "integral to the development and verification of [the project's] business plan" (L.J.A. BI-5) and "implementation plan" (L.J.A. CD); that UIH "contributed significant network, financial and managerial input and . . . acted as Wharf's 'agent' in securing and vetting key personnel" (L.J.A. CU-1); and that Wharf "relied heavily on UIH [for help] . . . [in its] procurement of technical design resources, equipment and personnel" (L.J.A. CW-2). *See also* L.J.A. CM; DD. At trial, there was evidence, for example, that certain of UIH's advice on equipment saved Wharf $66 million (*see* J.A. EC-1-5), and that Wharf needed and derived enormous value from being allowed to use UIH's name in the license application and to represent to the BA, to Wharf's investors, and to the public that UIH was Wharf's "strategic partner" (*see, e.g.*, J.A. DW-59-60; DB-1-5; EI-1; DI-1-10; V-1-7; AR-21-22; DW-57-61, 66-67, 79-86, 101-111; L.J.A. AY-1; BD; BE; BF; BI; BK; BM; BQ; CD; *see also* J.A. EM-62; EP-10).

The sale of the Option was a fraud. Wharf's own documents showed that it never had any intention to allow UIH to invest and that on the date of the sale, when Ng, acting for Wharf, represented that UIH would have the right to exercise the Option for a six-month period after license award, he was lying. In September 1992, Wharf's Chairman, Peter Woo, had instructed Ng to get additional help, sending Ng a note that said, "[a]cquire technical expertise! . . . UIH on cable T.V." L.J.A. AI-2; J.A. DT-189. Ng had reminded Woo that in return for its "expertise!" UIH insisted on an investment right that would give UIH time to raise money to fund its share of the equity capital. *See* L.J.A. AI-1; J.A. DT-

57-58, 183-87. But Woo replied in a note, "No, no, no we don't accept that." J.A. DT-187. Facing the dilemma posed by these conflicting instructions, Ng took the easy way out: On October 8, he sold UIH the Option without disclosing that Wharf, ruled by Woo, had no intention of honoring it. *Compare* J.A. DK-219-23, 303-04 (Woo); BD-89-90, 97-99 (Ng) *with* J.A. T (Elsner); AF-9-13 (Schneider). The jury found that the deception was intentional and material and that UIH relied on it and was damaged. J.A. EP-1-5, 14-18, 28-32.

After October 8, Ng and Fung repeatedly assured UIH of its right to invest and continued to hold out UIH as its "partner." *See supra* pp. 8, 10. To support the credibility of its bid, Wharf introduced UIH's senior personnel to Hong Kong government officials. J.A. DI-4-10; DT-286-300; L.J.A. AW. Wharf also allowed UIH to talk to third parties about the Option in Wharf's presence without contradiction by Wharf. *See, e.g.*, J.A. BH-9-13, 18-21.

After May 1993, when the bid was awarded to Wharf effective June 1 (*see* L.J.A. CL), Ng immediately told Woo, "partnership discussions with UIH in suspension" (L.J.A. CN; CO; CQ-5). But Wharf still needed UIH's assistance (*see, e.g.*, J.A. BH-18-27), so Wharf said nothing to UIH and continued to purport to document UIH's investment rights and to discuss a possible new agreement under which UIH would acquire more than 10% (*see* J.A. BA; AU). Wharf kept "negotiating" the documentation, offering excuses why documents could not yet be signed. *See id.* As Mark Schneider described the process in hindsight, UIH was being "slow rolled." J.A. AU 3-4.

Wharf expected UIH to fail to raise the funds needed to execute the Option. Indeed, Woo had predicted, "they will fail!" L.J.A. AI-2. But by July 1993, UIH had completed a public stock offering that raised sufficient funds and informed Ng that it wanted to exercise the Option. *See* J.A. V-13-15; AL; BS-4; DK-403 (Woo concedes he knew that

UIH raised needed funds by summer 1993). Ng went to see Woo, who refused to allow this. *See* J.A. DW-140-42. Ng immediately wrote to Fung: "Didn't get very far with the Chāirman [Woo]. . . *How do we get out?*" L.J.A. CY (emphasis added). Ng and Fung then worked to "get out" of Wharf's obligations to UIH, offering for the first time excuses such as the false claim that UIH's rights were subject to NYNEX's involvement. *See* J.A. AM; L.J.A. CZ. Wharf documents show that its strategy was to "start to backpeddle" [*sic*] and later to "stall." L.J.A. DG-1; DJ-1. A November 1993 memo from Fung to Ng said, "Our next move should be to claim [to UIH] that our directors got quite *upset*" at UIH's investment rights (L.J.A. DF), but Fung admitted at trial that the claim of upset directors was false (*see* J.A. DO-1-5). Wharf also tried to get UIH to "take the bait" by accepting a fee in lieu of exercising its Option. *See* J.A. Q; AE; AO-11-17; BB; L.J.A. DH-1-2. Finally, in March 1994, Elsner and Schneider were allowed to meet with Wharf's board (*see* J.A. R; AP; CY); they told the board that UIH was "very pleased that we had this right to invest and we were glad to be partners with [Wharf] in this project," but two hours later Ng told them that Wharf was "not ready to entertain your investment at this time." J.A. R-1-5.

3. The Jury Instructions and the Jury's Verdicts.

The jury instructions defining a Rule 10b-5 violation and the verdict form asking the jury whether Wharf had sold UIH an Option were largely undisputed and were not challenged in the court of appeals. The jury returned a detailed special verdict finding Wharf liable under Rule 10b-5. The jury answered "YES" to the following question:

> Do you find that Wharf Holdings entered into a contract with UIH granting an option to purchase a 10% ownership interest in the Hong Kong cable project?

J.A. EP-7. The jury also answered "YES" to separate questions on (a) material deception in connection with this sale of a security (*see* J.A. EP-11), (b) scienter (*see* J.A. EP-12), and (c) reliance (*see id.*). On damages evidence whose admissibility was not challenged and an agreed damages instruction (*see* J.A. EM-72), the jury held Wharf liable for $67 million in compensatory damages (*see* J.A. EP-12).

The jury's instructions and decision regarding the existence of an oral contract. The jury expressly found that the parties intended to be bound by the October 8, 1992 oral agreement granting UIH the Option. *See* J.A. EP-7-9. There were lengthy agreed-to instructions (*see* J.A. EM-48-50) differentiating between (i) an oral agreement that is binding when entered into, although the parties intend later to record it in writing, and (ii) an oral agreement that the party to be charged does not intend to be binding until it is written down. The jury not only found that "Wharf Holdings entered into a contract with UIH granting an option" (J.A. EP-7), but also expressly rejected Wharf's claim that the parties did not intend to be bound without a writing (*see* J.A. EP-8-9).

The jury's instructions and decision regarding the existence of unfulfilled conditions. Wharf argued at length that there were unsatisfied conditions to UIH's right to exercise its Option. The jury received an unchallenged instruction on this point (*see* J.A. EM-53-54) and specifically found that any conditions to Wharf's "obligation to perform the contract have been fulfilled or excused" (J.A. EP-8).

The jury's instructions and decision bearing on "enforceability." Wharf argued at trial that the contract granting UIH an Option was not enforceable under a since-repealed Colorado statute of frauds, *see* Colo. Rev. Stat. § 4-8-319.[9] As both courts below noted, under Colorado law, the

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[9] Former Colo. Rev. Stat. § 4-8-319 was based on former Uniform Commercial Code § 8-319. U.C.C. § 8-319 was repealed after UIH brought suit, and it has been replaced in every State by U.C.C. § 8-113,

statute did not apply where the party seeking to enforce the contract provided "substantial part performance." As the court of appeals stated, there was no dispute "that UIH substantially, and most likely fully, satisfied its obligations [to assist Wharf]." Pet. App. B-24. The question, under Colorado law, was whether UIH's services were "fairly referable" to the oral contract or were explained on an alternative basis, such as Wharf's theory that UIH was acting as a hopeful volunteer. The jury was given a specially crafted instruction *requested by Wharf* (*see* 1/10/97 Trial Preparation Conf. Tr. at 59:25-60:4) on that issue:

> If you find that in exchange for the option, UIH promised to provide any services to the defendant, then you must find that there was consideration.
>
> If [UIH], however, did or promised to do nothing more than it was already obligated to do, or was working voluntarily for its own benefit, then no consideration is present and you must find for the defendants.

J.A. EM-46. So instructed, the jury found that Wharf "entered into a contract with UIH granting an option." J.A. EP-7.

The evidence, instructions, and verdicts on the state law claims. There was no pertinent dispute at trial about the admission or exclusion of evidence bearing on the claims of common law fraud or breach of fiduciary duty to a joint

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which reads, "[A] contract . . . for the sale or purchase of a security is enforceable whether or not there is a writing signed or record authenticated by a party against whom enforcement is sought . . . ." Colo. Rev. Stat. § 4-8-113; U.C.C. § 8-101 (amended 1994), U.L.A. U.C.C. Prec. § 8-101, Refs. & Annos., "Adoption of 1994 Revision of Article 8" (Supp. 2000) (at time of publication, 48 states had adopted revised Article 8); 2000 R.I. Pub. Laws 00-420; S.C. Code Ann. § 36-8-319, *repealed by* 1999 Act No. 42, § 4, eff. June 1, 1999 (now at S.C. Code Ann. § 36-8-113). *Every State now treats oral sales of securities as valid and enforceable without a writing. Cf.* Pet. App. B-22 n.2.

venture partner (which rested on the entire two-year period of obtaining help with false promises of investment rights and other malfeasance toward Wharf's "strategic partner"), or on breach of contract or negligent misrepresentation, all under Colorado law. The instructions defining these claims were essentially agreed to, and were not challenged on appeal. The jury found Wharf liable on each claim. *See* J.A. EP-1-11.

The jury's instructions and decision regarding damages. An option to purchase 10% of the stock of the owner of the exclusive franchise to provide cable TV in one of the world's great cities was valuable. At trial, UIH presented, *inter alia*, expert testimony that the "value lost by UIH"—the difference between the value of the Option had it been as represented and its value given Wharf's fraud—was $67 million. *See* Aplt. App. 8187:6-232:11 (credentials); 8272:16-273:3; 8232-342; 8512-519. Wharf did not dispute the expert's qualifications, or the admissibility of his testimony or of any other UIH evidence on damages.[10] The parties agreed on the jury instructions defining the measure of damages on each claim. The jury returned separate verdicts of $67 million on the claims of securities fraud, common law fraud, breach of fiduciary duty, and breach of contract. *See* J.A. EP-4, 9, 10, 13, 18, 22, 24, 26, 31, 34.[11]

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[10] UIH presented a second expert who testified to the correctness of the methodology of the first (*see* Aplt. App. 9824:10-832:4; 9850-853; 9852-892); an internal witness who testified that UIH's estimate of the value of its Option, before Wharf won the franchise, had been more than $50 million (*see* J.A. CW-13-14); and an analyst's report from an (unrelated) underwriting firm that had valued the right at $56.6 million (*see* J.A. CT-2-4; L.J.A. DA-8).

[11] *Six months after trial*, at the hearing on post-trial motions in the district court, Wharf first accused UIH counsel of misrepresenting its damages expert's testimony in closing argument to the jury. Wharf repeats the accusation in this Court *See* Br. 14, 20 ("brazenly misrepresented"). This goes well beyond the bounds of responsible advocacy. Not only did Wharf fail to object to either the testimony or the

B. Proceedings in the Court of Appeals.[12]

The Tenth Circuit affirmed. The court first determined that the district court had subject matter jurisdiction, noting that a court has jurisdiction under 28 U.S.C. § 1331 if the complaint alleges a substantial federal claim, and that a claim is insubstantial "only if it is 'obviously without merit or is wholly frivolous,' or 'is clearly foreclosed by prior decisions of the Supreme Court.'" Pet. App. B-13 (citation omitted). It held that, once a district court has such jurisdiction, its supplemental jurisdiction under 28 U.S.C. § 1367(a) "does not fluctuate with the fate of [the] federal claim at trial or on appeal" (Pet. App. B-13); on the contrary, "[o]nce a trial is held . . . this court will order dismissal of a pendant claim on remand only when the federal cause of action was so insubstantial and devoid of merit that there was no federal jurisdiction to hear it," *id.* (citation omitted).

Turning to UIH's Rule 10b-5 claim, the court said, "[W]e are convinced that UIH's allegations not only are substantial and nonfrivolous, but state an actionable 10b-5 claim . . . ." Pet. App. B-15. The court first ruled that the claim involved a "security": "UIH has asserted throughout this case, *without challenge from Wharf*, that the security for 10b-5 purposes is not the [CNCL] stock but is the option

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closing argument during the trial (*see* Pet. App. B-30-31), its argument (on which this Court did not grant certiorari) is completely wrong: as the Tenth Circuit explained, the expert *did* subtract the money that UIH would have had to invest to exercise the Option, the amount about which Wharf is arguing, and the expert's calculation of UIH's loss was correct. *See id.* at B-31-32. Wharf is seeking a double subtraction of the same investment. *See id.*

[12] This was Wharf's third appeal. The Tenth Circuit had previously affirmed denial of a motion to compel arbitration (No. 95-1184 (Feb. 9, 1996), *cert. denied sub nom. Wharf Cable Ltd. v. United Int'l Holdings, Inc.*, 518 U.S. 1005 (1996)) and denied a petition for a writ of mandamus (No. 97-1423 (Nov. 14, 1997)). A related appeal by Wharf unsuccessfully sought to overturn contempt sanctions that the district court entered against Wharf Holdings (No. 98-1002 (Apr. 28, 2000)).

itself.... *Wharf does not contest on appeal the classification of the option as a security.*" *Id.* (emphasis added). The court then noted that the complaint "allege[d] that the option was purchased by UIH on October 8, 1992, in exchange for its continued and expanded assistance to Wharf in the pursuit of its cable bid." *Id.* Thus, the court ruled, "UIH was an actual purchaser [of a security] . . . from Wharf on October 8, 1992 [and] *Blue Chip* [*Stamps v. Manor Drug Stores*, 421 U.S. 723 (1975)] does not preclude UIH's 10b-5 claim." Pet. App. B-16.

The court noted that UIH had alleged that Wharf made material misrepresentations and omissions in connection with the sale of the security, either "with knowledge of their falsity or with reckless disregard for their truth or falsity." Pet. App. B-15. It held that the "in connection with" requirement was satisfied because the "misrepresentations were made to influence UIH's investment decision [to purchase the Option with its services]." *Id.* at B-16. It agreed with decisions of the Second, Third, and D.C. Circuits that entering into a contract to sell a security "with a secret reservation not to fully perform" is fraud barred by Rule 10b-5. *Id.* at B-16-17. The court distinguished Wharf's cases as involving mere breaches of contract, not misrepresentations of intent at the time of sale. *See id.* at B-17.

In the Tenth Circuit, as here, Wharf devoted much of its brief to attempting to overturn the jury's finding that on October 8, 1992, Wharf entered into a contract granting UIH an Option. The court found "ample" evidence supporting UIH's allegations. *See* Pet. App. B-28. The court singled out the testimony of UIH officials "that Ng specifically granted such an option in exchange for UIH's continued and expanded provision of services to Wharf." *Id.* The court also noted corroborating evidence in the record. *See id.*

The Tenth Circuit also rejected Wharf's other challenges. It explained that Wharf's choice-of-law argument had no bearing on the district court's jurisdiction or

on the outcome of the case: "[T]he crux of UIH's 10b-5 claim is the October 8, 1992, meeting between Wharf and UIH in Denver, Colorado. The security was sold at that meeting, the negotiations for the sale occurred at that meeting, and the most material of Wharf's misrepresentations were made at that meeting." Pet. App. B-19.

The court next rejected, on two different grounds, Wharf's claim that the former Colorado statute of frauds applicable to some sales of securities, *see* Colo. Rev. Stat. § 4-8-319 (repealed), made the purchase of the Option unenforceable: the Option was not a "security" within the narrow technical definition in the former statute, and in any event the state-law exception for contracts that have been partially performed removed the case from the statute of frauds altogether. Noting that "Wharf does not dispute the assistance rendered by UIH," Pet. App. B-24, the court rejected Wharf's contention that the jury should have been asked an additional question to determine whether UIH's performance was pursuant to the Option contract or merely, as Wharf contended, "in the hope of persuading Wharf to sell it 10% of CNCL stock." *Id.* The court held that the jury *was* asked that question and the court could "discern no prejudice to Wharf." Pet. App. B-24-25.

The court also carefully examined the Colorado cases and rejected, on two different grounds, Wharf's argument that Colorado's "economic loss rule" doctrine precluded UIH's common law fraud and breach of fiduciary duty claims. The Colorado rule "applies only to tort claims based on negligence," Pet. App. B-26, and only when "'the duty breached is a contractual duty,'" *id.* (quoting *Jardel Enters., Inc. v. Triconsultants, Inc.*, 770 P.2d 1301, 1303 (Colo. Ct. App. 1988)). The court noted that the Colorado rule does not apply to a fraud inducing the plaintiff to enter into a contract or to a breach of fiduciary duty to a joint venture partner. *See* Pet. App. B-26-27.

Finally, the court rejected challenges to the sufficiency of the evidence of compensatory and punitive damages. On the latter, it noted that "ample evidence" supported the jury's finding of "fraud, malice, or willful and wanton conduct":

> The jury necessarily found that on October 8, 1992, Ng agreed to grant UIH a 10% option, knowing even then that Wharf would not allow UIH to exercise that option. Wharf's internal memos in particular not only evidence Wharf's deliberate misrepresentations regarding the existence of UIH's option, but also reveal Wharf's internal generation of fabricated excuses and purposeful implementation of stall tactics in its subsequent dealings with UIH.

Pet. App. B-36.

SUMMARY OF ARGUMENT

I. UIH pled and proved every element of a Rule 10b-5 claim. The Option was itself a "security" as defined in Section 3(a)(10) of the Exchange Act, 15 U.S.C. § 78c(a)(10). Wharf sold that security to UIH on October 8, 1992, and UIH promptly paid the purchase price by "seconding" its own senior personnel to work for Wharf at UIH's expense and providing other requested assistance. Wharf deliberately and materially deceived UIH in connection with the sale, representing on October 8, 1992 that UIH would have the right to exercise the Option during a specified period, when in fact, on that date, Wharf did not intend to honor the Option. UIH relied on this deception to its detriment. The jury explicitly found each of these facts. *See* J.A. EP-7, 11-13.

Wharf's central argument, based on *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723 (1975), rests on factual assertions that the jury specifically rejected. Wharf contended at trial that there was no actual sale of the Option on October 8 but only a long period of unsuccessful

negotiations, during which UIH provided its large and indispensable assistance to Wharf as a volunteer, merely hoping for an investment opportunity. But the jury explicitly found that Wharf "*entered into* a contract with UIH *granting* [UIH] an option to purchase a 10% ownership interest in the Hong Kong cable project" J.A. EP-7 (emphasis added), and the Tenth Circuit found substantial evidence to support the jury's finding. It is entirely inappropriate for Wharf to premise a *Blue Chip* argument on the factual assertion that UIH was not an "actual purchaser" when the jury expressly found to the contrary. And since UIH was an "actual purchaser," Wharf's cases that involve contract disputes rather than actual sales are not in point.

UIH's Rule 10b-5 claim is also wholly consistent with the "rationale" of *Blue Chip*. As later described by this Court itself, the Court's central concern in that case was the potential for strike suits if plaintiffs could base their claims on *hypothetical* transactions that they decided *not* to pursue, because those claims will often turn on untestable assertions about a plaintiff's state of mind. Actual transactions, including oral ones, present no such problem, because the key facts are necessarily external: the plaintiff will be required to prove, as UIH did here, that statements were actually made at a particular time and place to effect a sale; there will be provable payments and other actions taken by various persons as a direct result; and of course the plaintiff will have to "connect" the defendant's false representations to the "actual sale." Unlike testimony centered on "the state of [the plaintiff's own] mind," *Blue Chip*, 421 U.S. at 744 (internal quotations omitted), the testimony and other evidence proving such external facts will be testable through cross examination, the testimony of other persons present, and other evidence. Since oral sales of securities are enforceable in every State, a new ruling by this Court that such sales do not "count" for Rule 10b-5 purposes would remove a substantial category of fraudulent transactions from the ambit of the Rule.

Wharf's all-but-abandoned argument that the defendant's misrepresentation must relate to "financial information" or to the "value" of the security is both irrelevant and wrong. It is irrelevant because Wharf's misrepresentation here *did* go to the value of the Option: while the Option as represented had a (jury-determined) value of $67 million, in reality the Option was worthless, since Wharf never intended to permit its exercise. The argument is also wrong, because a large number of cases in both this Court and the courts of appeals have upheld Rule 10b-5 claims where the misrepresentation had nothing to do with either financial information or value.

II. The judgment for UIH in this case does not depend on the answers to the two Rule 10b-5 questions before the Court. UIH pleaded and proved, and the jury found, in detailed special verdicts, that Wharf had committed both common law fraud and breach of fiduciary duty to a joint venture partner, and the jury awarded the full amount of damages on each of these counts. Either of these awards is therefore sufficient to sustain the entire judgment. Wharf's suggestion that the Tenth Circuit incorrectly resolved two Colorado law questions (on which the Court did not grant certiorari) in connection with these verdicts is baseless; the supposedly conflicting cases from other circuits do not interpret Colorado law, which is clear on both points.

Wharf's suggestion that a Wharf victory in this Court on its Rule 10b-5 argument would mandate dismissal of the state law verdicts is groundless. Since UIH's Rule 10b-5 claim was clearly substantial as pled, a rejection of that claim now on the merits would not disturb the federal courts' jurisdiction to hear this case. Dismissal of the pendent claims would be discretionary, turning on "considerations of judicial economy, convenience and fairness to litigants," and taking "the already completed course of the litigation" into account. *United Mine Workers v. Gibbs*, 383 U.S. 715, 726-27 (1966). Each of these factors, as well as every one of a

long string of precedents, stands in opposition to rejecting the otherwise valid state-law verdicts nearly four years after an 11-week, 39-witness trial.

ARGUMENT

I. UIH PLED AND PROVED A VALID CLAIM UNDER RULE 10b-5.

The Tenth Circuit's ruling that "UIH's allegations . . . state[d] an actionable 10b-5 claim," Pet. App. B-15, was correct. UIH pled and proved every element of such a claim. The jury's verdict is consistent with both the letter and the "rationale" of *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723 (1975). Wharf seeks to create a new exception that would render Rule 10b-5 inapplicable to securities sales that are common and enforceable in all fifty States.

A. UIH Pled and Proved Each Element of a Rule 10b-5 Claim.

1. The Option was a security. UIH's Complaint pled that "the grant of the option . . . was the sale of a security to [UIH], within the meaning of the Securities Exchange Act." J.A. F-22. As the court of appeals noted, "UIH has asserted throughout this case, without challenge from Wharf, that the security for 10b-5 purposes . . . is the option itself." Pet. App. B-15; *see also* J.A. F-22. Moreover, "Wharf [did] not contest [below] the classification of the option as a security." Pet. App. B-15. The Exchange Act defines "security" to include "any . . . option," 15 U.S.C. § 78c(a)(10), as this Court recognized in *Blue Chip*, 421 U.S. at 751, and as other courts have made clear. *See One-O-One Enters., Inc. v. Caruso*, 848 F.2d 1283, 1288 (D.C. Cir. 1988) (R. Ginsburg, J.) (right to purchase securities, whether an "option" or a contract right is itself a security).[13]

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[13] *See also Fry v. UAL Corp.*, 84 F.3d 936, 938 (7th Cir. 1996) ("stock options are securities" under the Exchange Act); *Mansbach v. Prescott,*

2. Wharf sold this security to UIH, which was an "actual purchaser." UIH's Complaint pled in detail that on October 8, 1992, Wharf actually sold UIH an option, on specific terms, to purchase 10% of the stock of CNCL. *See* J.A. F-13-15. UIH proved the sale through the testimony of two witnesses present at the meeting where the sale occurred (*see, e.g.*, J.A. P-6-23; U-2-7; AF-1-13), which was corroborated by evidence of statements and actions immediately after the meeting (*see, e.g.*, J.A. AT-1-9; AR; BO-36-45; DB-22-28; V; DI-4-10; BH-7-27; CQ; CK; CT-1-4; L.J.A. BD; BE; BF; BG; BH; BJ-4; BK; BP-1, 18; CT-1), and by written evidence and testimony (including documents from the files of Wharf, UIH, and third parties) that the parties were discussing an "option" before that meeting and that UIH held an "option" and had "investment rights" after the meeting (*see, e.g.*, J.A. BM-5-10; P-3-8; BH-1-9; BO; DW-51-52; V; BH-9-27; BI-1-4; BS; BR; CT; R-3; L.J.A. D; L; T-17; AK-2; AL; AN-2; AP-1; AO-1; BG; BP-1, 18; CG-4; CH-1; CK-4; CT; DA-8). UIH also provided evidence of Wharf's desperate attempts to "get out" of its obligations to UIH, which further demonstrated its recognition of UIH's Option rights. *See supra* p. 12. The jury received detailed uncontested instructions on oral contracts (*see* J.A. EM-40-56) and expressly found that such a contract existed here (*see* J.A. EP-7-9, 21-22).

3. In connection with this sale, Wharf deliberately deceived UIH about a highly material fact. UIH's Complaint pled that Wharf, through Ng, represented that UIH would have the right to exercise the Option and that "[t]hese representations were false when made." J.A. F-22-23. The evidence, including materials from Wharf's files, showed that as of October 8, 1992, Wharf did not intend to allow the Option to be exercised. *See supra* pp. 10-11. This is a more than sufficient basis for a Rule 10b-5 claim. "[F]raud in the

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Ball & Turben, 598 F.2d 1017, 1026 n.40 (6th Cir. 1979) (Securities Act definition "clearly includes options to purchase or sell stock").

purchase or sale includes entering into a contract of sale of a security with the secret reservation not to fully perform." *Threadgill v. Black*, 730 F.2d 810, 811-12 (D.C. 1984).[14] For example, a buyer (or seller) who intends, when he enters into a contract to purchase or sell a security, to honor it only if the price goes up (or down) commits a classic fraud in violation of Rule 10b-5. *See A. T. Brod & Co. v. Perlow*, 375 F.2d 393, 397 (2d Cir. 1967).[15] The Complaint also expressly alleged scienter and materiality (*see* J.A. F-23), and the jury expressly found that Wharf "acted knowingly" (*see* J.A. EP-12) and that the fraud was "material" (*see* J.A. EP-11).

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[14] *See Hill v. Hanover Energy*, No. Civ. A. 91-1964, 1991 WL 285295, at *5 (D.D.C. Dec. 16, 1991) (mem.); *Madison Consultants v. FDIC*, 710 F.2d 57, 66 (2d Cir. 1983); *In re Phillips Petroleum Secs. Litig.*, 881 F.2d 1236, 1245 n.13 (3d Cir. 1989); *Luce v. Edelstein*, 802 F.2d 49, 56 (2d Cir. 1986); *McGrath v. Zenith Radio Corp.*, 651 F.2d 458, 466-67 (7th Cir. 1981) (security sold through false promise of future promotion); *Walling v. Beverly Enters.*, 476 F.2d 393, 396 (9th Cir. 1973) ("Entering into a contract of sale with the secret reservation not to fully perform it is fraud cognizable under § 10(b)."); *see also Klorer v. Bennett*, 907 F.2d 150 (table), 1990 WL 94241, at *6 (6th Cir. July 9, 1990) (recognizing same); *cf. Messer v. E.F. Hutton & Co.*, 847 F.2d 673, 677 (11th Cir. 1988) ("false promise to perform future services can support a claim under the [Commodity Exchange Act] antifraud provisions").

[15] This doctrine of federal securities law parallels the black-letter state law of fraud. "A representation of the maker's own intention to do or not to do a particular thing is fraudulent if he does not have that intention." Restatement (Second) of Torts, § 530 (1976).

> [This] rule . . . finds common application when the maker misrepresents his intention to perform an agreement made with the recipient. The intention to perform the agreement may be expressed, but it is normally merely to be implied from the making of the agreement. Since a promise necessarily carries with it the implied assertion of an intention to perform it follows that a promise made without such an intention is fraudulent and actionable in deceit . . . . This is true whether or not the promise is enforceable as a contract.

Id., cmt. c.

4. UIH immediately paid the price for the Option in reliance on Wharf's deception. The Complaint alleged substantial reliance. *See* J.A. F-15-16, 24. Wharf was seeking immediate help and continuing use of UIH's name, reputation, and expertise. *See supra* pp. 7, 9-10. At the October 8 meeting, UIH said it would not provide this help, and would notify the Hong Kong BA that it was no longer associated with the project, unless Wharf, then and there, sold it the Option. *See* J.A. P-15-22; AF-4-7; AW-1-3. After Wharf did so, UIH, *inter alia*, immediately dispatched the requested personnel, at its own expense, to serve as the Chief Operating Officer and Chief Engineer of the project. *See supra* pp. 8, 9-10. The jury found that "UIH justifiably relied upon Wharf Holdings' conduct." J.A. EP-12.[16]

5. UIH was damaged. The Complaint alleged (J.A. F-24) and the jury expressly found, based on evidence and damages instructions that were unchallenged at trial, that UIH suffered damages as a result of Wharf Holdings' securities fraud. *See* J.A. EP-12; *see also* J.A. EP-26, 33.

B. UIH Was an "Actual Purchaser" of a Security as Required by *Blue Chip* and Wharf Defrauded UIH "In Connection With" the Sale.

In *Blue Chip*, this Court adopted the "*Birnbaum* rule" that only an actual purchaser or seller may bring a claim

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[16] Wharf does not dispute that services may be the purchase price of a security, including an option. *See, e.g., One-O-One Enters.*, 848 F.2d at 1285 (promise of services may be consideration for the sale of a security); *see also Gurwara v. LyphoMed, Inc.*, 937 F.2d 380, 383 (7th Cir. 1991) ("The mere fact that [plaintiff's] consideration took the form of accepting employment instead of pecuniary remuneration matters not at all."). The price paid in services to *obtain* the Option was distinct from the price—10% of the capital investment in CNCL—that UIH would have had to pay to *exercise* the Option and obtain CNCL stock; UIH proved that it conducted a public offering, raised sufficient funds, and told Wharf it was prepared to make the required capital investment and purchase the 10% interest. *See* J.A. V-13-15; AL; BS-4.

under Rule 10b-5. *See* 421 U.S. at 749. The Tenth Circuit acknowledged and applied that rule: "Here, UIH was an actual purchaser [of a security] as it purchased the option from Wharf on October 8, 1992. *Blue Chip* does not preclude UIH's Rule 10b-5 claim." Pet. App. B-16. Indeed, as noted in *Blue Chip*, the Tenth Circuit had adopted the *Birnbaum* rule ahead of this Court. *See* 421 U.S. at 731-32 (citing *Jensen v. Voyles*, 393 F.2d 131 (10th Cir. 1968)). No Tenth Circuit opinion, including the opinion in this case, has suggested any departure from *Birnbaum* or *Blue Chip*.

Wharf seeks to evade the actual holding of *Blue Chip* by ignoring the sale of the Option and asserting, over and over, that this case involves only a dispute about the right to acquire the underlying CNCL stock. Of course, since an option is by definition the right to buy (or sell) a distinct "underlying" security, a dispute about the sale of an option to the plaintiff is *also* a dispute about the plaintiff's right to buy (or sell) the underlying security. But an option is *itself* a security, and a deliberate and material lie in connection with a sale of that security violates Rule 10b-5. Here, Wharf defrauded UIH when it sold the Option, because its representations in connection with that sale were false, and Wharf *also* committed a breach of contract when it later refused to honor the Option by conveying the underlying CNCL stock. In October 1992, UIH not only agreed to accept the Option but paid the purchase price by immediately providing the promised services. Wharf's argument is not an application of *Blue Chip* but a wholesale revision of the facts that UIH proved and the jury found.

The Tenth Circuit drew precisely the correct distinction between a mere contract dispute and a fraudulent sale of a security.

> [F]raud in the purchase or sale of a security includes entering into a contract to sell a security with a secret reservation not to fully perform the contract. It is a party's secret reservation not to fully perform

> a securities contract that distinguishes these cases from routine breach of contract and common law fraud cases and brings them within the scope of Rule 10b-5.

Pet. App. B-16-17 (citations omitted); *see also Richardson v. MacArthur*, 451 F.2d 35, 40 (1971) ("[Rule 10b-5 is the] proper civil remedy for a scheme whereby individuals were induced into contracting for the purchase of stock which the seller had no intention of giving up").

Every other court of appeals to address this issue since *Blue Chip* has reached the same conclusion. For example, in *Luce*, 802 F.2d at 56, the Second Circuit explained:

> While the failure to carry out a promise made as consideration for a sale of securities . . . does not constitute fraud if the promise was made with a good faith expectation that it would be carried out . . . [p]lausible allegations that defendants made specific promises to induce a securities transaction while secretly intending not to carry them out or knowing they could not be carried out, and that they were not carried out, are sufficient . . . to state a claim for relief under Section 10(b).

The D.C. Circuit reached the same conclusion in *Threadgill*, 730 F.2d 810 (per curiam, Wright, Wilkey, and Scalia, JJ.). The district court had dismissed a Rule 10b-5 claim alleging that the defendant had orally agreed to purchase plaintiff's shares "without any intention of ever paying the full [price]," holding that since the defendant had reneged, "no actual sale or purchase of any security had taken place." *Id.* at 811. The court reversed, explaining:

> That was error. The "purchase or sale" of any security under [Section 10(b)] includes "any contract" to purchase or sell a security. Thus, fraud in the purchase or sale includes "[e]ntering into a contract of sale of a security with the secret

> reservation not to fully perform." There is no exception for oral contracts, and summary judgment for the defendant has been denied on facts almost identical to those alleged here. [Plaintiff] did not allege that he "negotiated" or "attempted" to sell his stock, but that he "entered into an agreement" of sale with appellees. Appellees denied that assertion, creating a contested issue of material fact which could not be resolved [without a trial].

Id. at 811-12 (citations of *Blue Chip* and other cases omitted); *see also* cases cited *supra* p. 23-24 & n.14.

Wharf's principal case on this issue, *Gurwara v. LyphoMed, Inc.*, 937 F.2d. 380 (7th Cir. 1991), suggests precisely the same point. Plaintiff there was told, falsely, that a termination for disability would not affect his options to buy his employer's stock. When, after termination, he attempted to exercise the options, he was refused as ineligible. The Seventh Circuit rejected his Rule 10b-5 claim because the misrepresentation was not "in connection with" any sale of the stock, which never occurred. But the court itself noted the distinction that governs here:

> Whether [plaintiff] might have sued successfully under section 10(b) for misrepresentations in connection with [an] *option contract* is an issue we need not resolve. Throughout this lawsuit, [plaintiff] has clearly relied on the LyphoMed stock itself as the "security" on which his 10(b) action was based.

Id. at 382 n.2.

Hunt v. Robinson, 852 F.2d 786 (4th Cir. 1988), *Tully v. Mott Supermarkets, Inc.*, 540 F.2d 187 (3d. Cir. 1976) and *Stanford v. Humphrey*, 894 F.2d 410, 1990 WL 4659, *1 (9th Cir. Jan. 25, 1990), are similarly irrelevant. Each involved claims of simple breach of contract, not fraud in connection with a completed sale. In *Hunt*, the plaintiffs challenged

"defendants' refusal to tender the shares as required by the terms of the contract." 852 F.2d at 787. In *Tully*, "[t]he fraud which plaintiffs have alleged lies not in the actual sale of stock to them, but rather in the refusal to sell the remaining Class A shares in accordance with the 1966 agreement [giving them a right of first refusal]." 540 F.2d at 194. In *Stanford*, a brief unpublished decision relying on *Hunt*, the alleged fraud revolved "around the employer's alleged failure to honor the terms of the employment contract. [Plaintiff] *neither alleged nor show[ed]* any causal connection between the employer's putative fraud and the purchase or sale of any security." 1990 WL 4659, at *1 (emphasis added). None of these cases' plaintiffs alleged or proved that he was deceived—as UIH was—into purchasing and paying for securities where, at the time of sale, the defendant had a "secret reservation" not to perform.[17]

Wharf argues, citing *Kagan v. Edison Bros. Stores, Inc.*, 907 F.2d 690 (7th Cir. 1990), and *Pelletier v. Stuart-James Co.*, 863 F.2d 1550 (11th Cir. 1989), that UIH had no Rule 10b-5 claim because its rights were "unenforceable" under the since-repealed Colorado statute of frauds that used to cover some sales of securities, *see* Colo. Rev. Stat. § 4-8-319.[18] But as both courts below held, UIH's Option *was*

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[17] Wharf's reliance on *Santa Fe Industries v. Green*, 430 U.S. 462 (1977), is equally inapposite. *Santa Fe Industries* holds that Rule 10b-5 does not "reach breaches of fiduciary duty by a majority . . . shareholder[] *without any charge of misrepresentation or lack of disclosure*." 430 U.S. at 470 (emphasis added and internal quotations omitted). But in this case, UIH pled and proved and the jury found a deliberate and material deception in connection with the sale of a security. Nothing in *Santa Fe* suggests that such a deception does not "count" merely because the misconduct is also fraud under state law. *Cf.* Section 28(a) of the Exchange Act, 15 U.S.C. § 78bb(a) ("rights and remedies provided by this chapter shall be in addition to any and all other rights and remedies that may exist at law or in equity").

[18] As the Tenth Circuit noted, Colorado law now provides that a "'contract for the sale or purchase of a security is enforceable whether or

enforceable, and *Kagan* and *Pelletier* are simply irrelevant, because (1) Colo. Rev. Stat. § 4-8-319 had no application to the sale of the Option because the Option was not a "security" within the narrow, technical definition of that statute (*see* Pet App. B-21-23) and (2) in any event, under Colorado law, UIH's "substantial part performance" (in fact, full performance) made the statute inapplicable.[19] Wharf has never disputed either that Colorado law contains an exception to the statute of frauds for substantial part performance (*see* Pet. App. B-24 (citing *Nelson v. Elway*, 908 P.2d 102, 108 (Colo. 1995))),[20] or that UIH provided substantial services to

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not there is a writing.'" Pet. App. B-22 n.2 (quoting Colo. Rev. Stat. § 4-8-113). All states now have similar provisions. *See supra* n.9.

[19] The district court (J.A. EL-3-4) noted additional applicable Colorado law exceptions to the statute of frauds including "fraud," "payment" for the security, and estoppel, none of which the Tenth Circuit reached. Pet. App. B-23; *See Brody v. Bock*, 897 P.2d 769, 774 (Colo. 1995) (Colorado courts "have long recognized the principle that the statute of frauds should not be permitted to be an instrument of fraud"); *Ellis Canning Co. v. Bernstein*, 348 F. Supp. 1212, 1229, 1232 (D. Colo. 1972) (rejecting statute of frauds defense under Colo. Rev. Stat. § 4-8-319 where defendant misled plaintiff to obtain "know-how" and gained "[t]he retention and enjoyment of the benefits of the bargain") (internal quotations omitted); *In re Doerfer's Estate*, 67 P.2d 492, 494 (Colo. 1937) (statute of frauds is not applied to shield a fraud); *see also Leisure Am. Resorts, Inc. v. Knutilla*, 547 So.2d 424, 427 (Ala. 1989) (statute inapplicable "because of jury's finding of fraud in the inception of the contract") *cited with approval in Brody*, 897 P.2d at 774; *Fisher v. First Stamford Bank & Trust Co.*, 751 F.2d 519, 523 (2d Cir. 1984) (payment); *Kiely v. St. Germain*, 670 P.2d 764, 767 (Colo. 1983) (estoppel). UIH proved the facts to support these exceptions as well.

[20] Wharf seriously misreads *Elway* in two respects. First, the *Elway* court held that performance there did not evidence the alleged oral contract because the same performance was already required by two prior *written contracts*, *see* 908 P.2d at 108-09; nothing in *Elway* suggests that a jury that has found a contract requiring specified performance must consider the possibility that the required performance was nevertheless voluntary. *See Knoff v. Grace*, 190 P. 526, 528 (Colo. 1920) (issue is whether performance is explained by "some contract other than that alleged"). Second, *Elway*'s discussion of conditional promises relates to

Wharf and raised the funds to exercise the Option. *See supra* pp. 9-10, 11-12.

Wharf's only argument is that the jury should have been asked whether the concededly substantial services were "fairly referable" to the Option contract only, rather than to Wharf's competing theory that UIH was a volunteer. On its face, this argument is illogical: the jury found that UIH and Wharf entered into a contract requiring UIH to perform certain services in exchange for the Option; Wharf's argument is that the jury might have found that UIH did "voluntarily" what the contract obligated it to do. But the short answer, as the Tenth Circuit explained, is that the jury *was* asked whether UIH performed under the contract or as a volunteer, and its answer was clear:

> [T]he partial performance exception precludes application of the statute of frauds. . . . The alleged oral agreement . . . required UIH to provide additional services to Wharf. It cannot be disputed that UIH substantially, and most likely fully, satisfied its obligations. Indeed, Wharf does not dispute the assistance rendered by UIH, but asserts the assistance was fairly referable to Wharf's theory that UIH performed services relating to the cable television contract in the hope of persuading Wharf to sell it 10% of the CNCL stock. . . . Wharf contends the district court improperly took this issue from the jury. . . .
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> We agree with the district court that Wharf's proposed instruction on partial performance was superfluous. The breach of contract instruction on

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a separate claim in that case based on promissory estoppel, *see* 908 P.2d at 109-10, and has nothing to do with the part performance doctrine. (Moreover, the jury found that the grant of the Option was not conditional. *See supra* p. 13; J.A. EM-53; EP-8, 21.)

> consideration precluded recovery on breach of contract if the jury found that UIH "in exchange for the option . . . did or promised to do nothing more than it was already obligated to do, or was working voluntarily for its own benefit." Because the jury found that consideration existed and the oral option agreement was valid, it necessarily concluded that UIH provided Wharf assistance in exchange for the option and not for an extraneous reason . . . .

Pet. App. B-24-25 (citation omitted). In sum, the court of appeals, reviewing the jury instructions as a whole,[21] determined that the jury necessarily found that UIH had substantially performed its part of the bargain—and had done so *as* part of the bargain—taking this case out of the statute of frauds as a matter of Colorado law.

Finally, it is not—and plainly should not become—a defense under Rule 10b-5 that the security fraudulently sold by the defendant had yet to be documented, or was somehow defective. As Judge Posner said in *SEC v. Lauer*, 52 F.3d 667 (7th Cir. 1995), "[I]t would be a considerable paradox if the worse the securities fraud, the less applicable the securities laws." *Id.* at 670. In *Lauer*, the court rejected the argument that no "security" was involved in a promotional scheme to invest in "'Prime Bank Instruments,' a nonexistent high-yield security." *Id.* at 669. The court held that the promotional scheme was an investment contract, and thus a security, even though the "Instruments" were fictitious and, because the promoters thus obviously could not have intended to invest in them, there was no "real" investment contract either. "It is the representations made by the promoters, not their actual conduct, that determine whether

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[21] *See United States v. Park*, 421 U.S. 658, 674-75 (1975) ("in reviewing jury instructions [for abuse of discretion], our task is also to view the charge itself as part of the whole trial"); *Hamling v. United States*, 418 U.S. 87, 107 (1974) ("jury instructions are to be judged as a whole").

an interest is an investment contract (or other security). . . . An elementary form of . . . misrepresentation is misrepresenting an interest as a security when it is nothing of the kind." *Id.* at 670; *accord SEC v. United Benefit Life Ins. Co.*, 387 U.S. 202, 211 (1967); *SEC v. C.M. Joiner Leasing Corp.*, 320 U.S. 344, 352-53 (1943). Rule 10b-5 applies to sales of securities that have not yet been issued, *see Sulkow v. Crosstown Apparel, Inc.*, 807 F.2d 33, 36 (2d Cir. 1986); to securities that are not in writing, *see Canadian Imperial Bank of Commerce Trust Co. v. Fingland*, 615 F.2d 465, 467 (7th Cir. 1980) ("a writing is not mandatory"); and to "securities" that turn out to be fictitious and thus unenforceable.[22] The definition of "security" in the Exchange Act does not require a writing and makes no exception for supposed "securities" that are not as they were represented to be. The Option Wharf sold to UIH was a security, based on Wharf's representations, even though the sale was proved to be a sham because Wharf had no intention to permit the Option's exercise.

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[22] *See, e.g., Harrison v. Dean Witter Reynolds, Inc.*, 79 F.3d 609 (7th Cir. 1996) (Ponzi scheme with nonexistent municipal bonds); *First Nat'l Bank v. Estate of Russell*, 657 F.2d 668, 673 n.16 (5th Cir. 1981) (violation even if the "security purportedly traded is nonexistent or fictitious") (internal quotations and citation omitted); *Lincoln Nat'l Bank v. Herber*, 604 F.2d 1038, 1040 (7th Cir. 1979) (sale of nonexistent securities); *Mishkin v. Peat, Marwick, Mitchell & Co.*, 744 F. Supp. 531, 553 n.10 (S.D.N.Y. 1990) ("The fact that the securities did not exist does not remove this action from the operation of the federal securities laws."); *see also United States v. Schlei*, 122 F.3d 944, 972 (11th Cir. 1997) (definition of "security" in 15 U.S.C. § 77b(a)(1) includes counterfeit and forged securities); 5B Arnold S. Jacobs, Litigation and Practice Under Rule 10b-5 § 38.03[a][i][J] at 2-179 (2d ed. Supp. 1997) ("Fraud would be fostered rather than deterred if nonexistent interests or forged instruments were exempted from the definition of 'security.'"). Wharf cites *Kagan* and *Pelletier* (Br. 33-39), but both are irrelevant to whether a defective security "counts" as a security for Rule 10b-5 purposes. The issue in those cases was not whether there was a "security" but whether an admittedly unenforceable executory contract is a "contract to sell" under Section 3(a)(14) of the Exchange Act, 15 U.S.C. § 78c(a)(14).

C. The Decision Below Is Entirely Consistent With the "Rationale" of *Blue Chip*.

Wharf argues that UIH's Rule 10b-5 claim is contrary to the "rationale" (*see* Br. 23) of *Blue Chip* because the grant of the Option was oral. But *Blue Chip* did not exclude oral actual transactions in securities, and extending it to do so now would remove the protections of Rule 10b-5 from actual purchases and sales that are enforceable under the law of every State. *Blue Chip* was concerned about the potential for vexatious litigation inherent in allowing claims based on a plaintiff's largely untestable assertions about his reasons for *not* engaging in a *hypothetical* purchase or sale. This case involves no such concern: the jury's verdict turned on external facts that were capable of proof or disproof, and were proved through oral testimony, cross-examination, and corroborating documents and circumstances.

The state law of every State now provides that a "contract . . . for the sale or purchase of a security is enforceable whether or not there is a writing . . . ." U.C.C. § 8-113.[23] Wharf is thus asking the Court to engraft a writing requirement that would make Rule 10b-5 inapplicable to frauds in connection with sales and purchases of securities that are enforceable in every State. Both before and since *Blue Chip*, the lower courts have repeatedly held to the contrary. "There is no exception for oral contracts." *Threadgill*, 730 F.2d at 812; *see also Tranchina v. Howard, Weil, Labouisse, Friedrichs, Inc.*, No. Civ. A. 95-2886, 1997 WL 472664, at *12 (E.D. La. Aug. 18, 1997) (undocumented sales of securities), *aff'd*, 145 F.3d 359 (5th Cir. 1998); *Chariot Group, Inc. v. American Acquisition Partners L.P.*, 751 F. Supp. 1144, 1149 (S.D.N.Y. 1990) ("an oral contract which reflects a meeting of the minds . . . is sufficient to confer 10b-5 jurisdiction"), *aff'd*, 932 F.2d 956 (2d Cir. 1991); *Desser v. Ashton*, 408 F. Supp. 1174, 1175 (S.D.N.Y.

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[23] *See supra* n.9.

1975) (oral agreement to purchase securities), *aff'd*, 573 F.2d 1289 (2d Cir. 1977); *Fogarty v. Security Trust Co.*, 532 F.2d 1029, 1034 (5th Cir. 1976) (oral agreement to purchase stock).

Blue Chip did not deny the validity of oral contracts or the admissibility of testimony to prove them. The Court's concerns centered on the strike-suit potential of claims based on untestable assertions of the plaintiff's mental reasons for *not* buying or selling. As the Court itself later described the case, "The root of [the Court's] concerns was a plaintiff's capacity to manufacture claims of *hypothetical* action, unconstrained by independent evidence." *Virginia Bankshares, Inc. v. Sandberg*, 501 U.S. 1083, 1092 (1991) (emphasis added). The Court feared "the potential for nuisance or 'strike' suits," *Blue Chip*, 421 U.S. at 740, if claims are allowed to depend on "rather hazy issues of historical fact," including "the state of a man's mind," *id.* at 743-44 (internal quotations omitted)—*i.e.*, his alleged reasons for an alleged decision *not* to act. The present case, involving deceit in connection with an actual sale, presents no such problem for at least three reasons:

First, although part of the proof of an actual sale may be oral testimony, that testimony (here and virtually always in the case of an actual sale) will attest to concrete external facts. Here, Messrs. Elsner and Schneider testified, as witnesses do every day, about what was *said* at a meeting that occurred at a particular time and place. They were extensively cross examined, and the jury was presented with corroborating testimony and documents. Ng testified (and was cross examined) about his contrary recollection (and lack of recollection). UIH's claim presented a triable issue because its witnesses testified to specific statements, and UIH won at trial because the jury believed them.

Second, here and virtually always in the case of an actual sale, the event had provable direct consequences. After the October 8, 1992 meeting, the participants made statements to

additional people (both within UIH and to third parties), who later testified to what they had been told, and UIH performed the services it had promised to Wharf in exchange for the Option. More generally, in the 11-week trial, UIH and Wharf presented to the jury a wide range of evidence on the central, disputed factual question: what transpired at the October 8 meeting. Wharf's problem is that the jury believed UIH's evidence.

Third, Wharf's fraud in connection with the sale was proved (as fraud in connection with an actual sale would normally have to be proved) by evidence going beyond the plaintiff's testimony. Wharf's own files and testimony from Wharf's own witnesses proved that Wharf had no intention, as of the time of sale (or thereafter), to honor the Option.

In sum, UIH's Rule 10b-5 claim fit the "rationale" as well as the letter of *Blue Chip*. UIH was an actual purchaser and based its claim on concrete external facts: a meeting, the defendant's statements, testimony and documents from the defendant showing that those statements were deliberately and materially deceptive, and statements and specific actions taken on the basis of what transpired at the meeting. UIH proved these facts with conventional, testable evidence. This was not (and could not have succeeded as) "vexatious" litigation; it was a suit to recover for an outrageous fraud.

D. Wharf's Argument That a Deception Must Relate to "Financial Information" or to the "Value" of the Security Sold Is Both Irrelevant and Wrong.

Wharf has all but abandoned its contention that a misrepresentation does not count, for purposes of Rule 10b-5, unless it relates either to "financial information" or to the "value" of the security. There are two good reasons for this.

First, the deception UIH proved in this case obviously *did* relate to the Option's value. Wharf misrepresented that it intended to honor the Option. If Wharf had so intended, the

Option would have had substantial value, proved at trial to be $67 million. But because of the deception, the Option was worthless. If there were really any requirement that the defendant's fraud relate to the value of the security sold, it is hard to imagine a case that would more clearly meet that requirement.

Second, no such requirement exists. Neither the words of Section 10(b)—which are the first and best guide to its meaning, *accord Blue Chip*, 421 U.S. at 733—nor the words of Rule 10b-5 impose any such limitation. And this Court and the courts of appeals have made it very clear that as long as a deliberately deceptive statement is made "in connection with" a sale or purchase and is "material" to the buyer or seller, there is a Rule 10b-5 violation regardless of what aspect of the transaction the statement refers to.

A recent example, which Wharf misleadingly describes (*see* Br. 28-29), is *SEC v. Jakubowski*, 150 F.3d 675 (7th Cir. 1998) (Easterbrook, J.), *cert. denied*, 525 U.S. 1103 (1999). The misrepresentation concerned the purchaser's identity, which was material to the seller because only certain persons were eligible to purchase the particular securities. The court flatly rejected the argument that a Rule 10b-5 claim lies only if "the misrepresentation concerns the value of the stock," *id.* at 679, holding that the "in connection with" requirement was satisfied because "Jakubowski made his statements directly to the issuer of securities, in order to induce the issuer to accept his offer to buy. How could there be a closer 'connection' . . . ?" *Id.* The "materiality" requirement was satisfied because the seller "would not have issued the stock had [it] known the identities of the real purchasers." *Id.* at 680.

The *Jakubowski* panel included Judge Cudahy, the author of the Seventh Circuit's earlier opinion in *Gurwara*, a case on which Wharf centrally relies for the "value" point. The *Jakubowski* panel's comment on the earlier case buries Wharf's argument:

> True enough, we wrote in *Gurwara* that the "misrepresentation . . . in no way related to the value of [the stock at issue]." 937 F.2d at 382. But this passage was irrelevant to the question whether the statements were "in connection with" a (nonexistent) purchase or sale. Dicta cannot control over the language of the statute.

Id. at 679.

As *Jakubowski* also noted, "If a misrepresentation must concern the value of the security in order to meet the 'connection' requirement, then [two of this Court's cases] were wrongly decided." *Id.* The court explained that in *United States v. O'Hagan*, 521 U.S. 642 (1997), this Court sustained a criminal conviction under Rule 10b-5 where the defendant's deception was "feigning fidelity" to a takeover bidder, 521 U.S. at 655, and did not relate to the value of the securities he bought. The *Jakubowski* panel also discussed *United States v. Naftalin*, 441 U.S. 768 (1979), in which this Court sustained a conviction under Section 17 of the Securities Act (whose language parallels Section 10(b) except that it proscribes fraud "in" rather than "in connection with" a sale of securities); the misrepresentation in *Naftalin* was that the defendant *owned* stock sufficient to cover a short sale—a representation that related not to value but to the buyer's risk that the seller might default. *See* 441 U.S. at 770.

The first case in which this Court recognized a private right of action under Rule 10b-5, *Superintendent of Insurance v. Bankers Life & Casualty Co.*, 404 U.S. 6 (1971), illustrates the same point. The securities at issue were U.S. Treasury bonds, for which the defendant buyer paid full price; the deception had nothing to do with the value of the bonds or the amount paid for them, but concerned the identity of the entity that would receive the purchase price. *See id.* at 9-10. Many cases in the courts of appeals have

likewise recognized Rule 10b-5 claims based on deceptions that did not relate to value or to financial information.[24]

II. THE JUDGMENT FOR UIH IN THIS CASE DOES NOT DEPEND ON THE ANSWERS TO THE RULE 10b-5 QUESTIONS PRESENTED TO THIS COURT.

In addition to its Rule 10b-5 claim, UIH pleaded and proved that Wharf committed both breach of fiduciary duty to a joint venture partner and fraud in violation of Colorado law. The jury's award of damages on each of these supplemental claims is sufficient to support the entire judgment. The validity of these awards (and the jury awards on other state law claims) does not depend on the Rule 10b-5 claim. A reversal of the Rule 10b-5 verdict on the merits would not call into question the district court's jurisdiction, since the claim as pled was clearly not frivolous. Since the district court had jurisdiction, the decision whether to retain the pendent state law claims would turn on "considerations of judicial economy, convenience and fairness," taking into account "the already completed course of the litigation." *United Mine Workers v. Gibbs*, 383 U.S. 715, 726, 727 (1966). As the Tenth Circuit held (*see* Pet. App. B-13-14), no precedent or logic would support nullifying virtually unchallenged state-law verdicts after six years of complex trial and appellate proceedings.

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[24] *See, e.g., Angelastro v. Prudential-Bache Sec. Inc.*, 764 F.2d 939, 943-44 (3d Cir. 1985) (failure to disclose interest rates on a margin account); *Marbury Mgmt., Inc. v. Kohn*, 629 F.2d 705, 710 (2d Cir. 1980) (misrepresentation as to expertise of brokerage firm employee); *A. T. Brod*, 375 F.2d at 397; *Richardson v. MacArthur*, 451 F.2d 35, 40 (10th Cir. 1971); *Hooper v. Mountain States Sec. Corp.*, 282 F.2d 195, 202-03 (5th Cir. 1960) (fraud related to consideration for the security); *see also Press v. Chemical Invest. Servs. Corp.*, 166 F.3d 529, 537 (2d Cir. 1999) (non-disclosure that Treasury bill proceeds would only be available days after maturity); *SEC v. Milan Capital Group, Inc.*, No. 00 Civ. 108(DLC), 2000 WL 1682761, at *2 (S.D.N.Y. Nov. 9, 2000) (misrepresentation of intent to complete contractual obligation).

A. The Judgment Below Rests Independently on the State Law Verdicts.

The jury's separate special verdicts finding Wharf liable for breach of fiduciary duty and fraud (*see* J.A. EP-1-5, 9-11), stand virtually unchallenged. Wharf does not dispute the admission, exclusion, or sufficiency of the evidence, or the jury instructions defining these claims or the relevant measures of damages. Wharf now obliquely suggests that two arguments—on the enforceability of the Option and the so-called "economic loss rule"—would defeat the state-law claims, but both suggestions are wrong.

Enforceability. Without any analysis or citation to Colorado law, Wharf asserts (*see* Br. 39) that its argument that the Option was unenforceable would, if accepted, defeat the Colorado tort claims as well.[25] But apart from the fact that the fraud claim was based on a two-year course of deceitful dealing going well beyond the sale of the Option (*see* J.A. EM-24-34; EP-1-5), the Colorado Supreme Court has squarely held that Colorado follows the rule of the Restatement (Second) of Torts, under which the misrepresentation of an intent to perform a promise is an actionable fraud "*whether or not the promise is enforceable as a contract.*"[26] *See Brody v. Bock*, 897 P.2d 769, 774-75 (Colo. 1995). None of Wharf's cases applies Colorado law;[27]

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[25] This flatly contradicts Wharf's position in the district court, where Wharf's counsel said, "I agree to this, that to make out a fraud claim, they would *not* have to show a contract. I agree with that. . . . And it's not clear under a breach of fiduciary duty claim whether they would be required to or not." 1/10/97 Trial Preparation Conf. Tr. at 12:12-22 (emphasis added). Wharf pled the statute of frauds, an affirmative defense, only as a defense to the breach of contract. *See* J.A. I-9, 11.

[26] Restatement (Second) of Torts, § 530, cmt. c (1976) (emphasis added); *see also supra* n.15.

[27] *See Pelletier v. Stuart-James Co.*, 863 F.2d 1550 (11th Cir. 1989) (Georgia law); *Gregg v. U.S. Indus., Inc.*, 715 F.2d 1522 (11th Cir. 1983)

indeed, Wharf cites one case the Colorado Supreme Court expressly declined to follow.[28] Moreover, the enforceability of the Option has no bearing on the verdict for breach of fiduciary duty to a joint venture partner. *See* J.A. EM-57-62 (jury instructions); EP-9-11 (verdict).

Economic loss rule. Wharf wholly failed to raise its economic loss rule argument in the district court.[29] The Tenth Circuit also properly rejected it on the merits, applying clear Colorado precedents. *See* Pet. App. B-26-28. Wharf's allegedly conflicting cases from other circuits are irrelevant because, *inter alia*, none applied Colorado law.

B. The District Court Had Jurisdiction Under 28 U.S.C. §§ 1331 and 1367 To Render the State-Law Verdicts.

Because UIH pled a substantial claim under Rule 10b-5, the district court had jurisdiction under 28 U.S.C. § 1331. None of Wharf's legal and factual defenses, even if successful, could deprive the district court of jurisdiction.

Wharf all but ignores the century of precedent establishing that a complaint properly pleading a colorable federal claim confers jurisdiction on the district court, which it retains even if the plaintiff's legal theory is rejected on the merits. *Steel Company v. Citizens for a Better Environment*, 523 U.S. 83 (1998), summarizes established law:

(Florida law); *Caplan v. Roberts*, 506 F.2d 1039 (9th Cir. 1974) (California law); *Cohen v. Pullman Co.*, 243 F.2d 725 (5th Cir. 1957) (Georgia law).

[28] *See Brody*, 897 P.2d at 775 (refusing to follow *Caplan v. Roberts*).

[29] In the district court, Wharf referred to the economic loss doctrine in its motion for summary judgment, but only in connection with a negligent misrepresentation claim that is not now at issue. *See* Aplt. App. 232. The rule was also briefly mentioned in the colloquy on jury instructions regarding that claim (*see id.* at 1289, 1290-96), and the court accepted the instructions Wharf proposed (*see id.* at 1297:21-22).

> It is firmly established in our cases that the absence of a valid (as opposed to arguable) cause of action does not implicate subject-matter jurisdiction, i.e., the courts' statutory or constitutional power to adjudicate the case. . . . [T]he district court has jurisdiction if the right of the [plaintiffs] to recover under their complaint will be sustained if the Constitution and laws of the United States are given one construction and will be defeated if they are given another, unless the claim clearly appears to be immaterial and made solely for the purpose of obtaining jurisdiction or where such a claim is wholly insubstantial and frivolous . . . .[i.e.] so insubstantial, implausible, foreclosed by prior decisions of this Court, or otherwise completely devoid of merit as not to involve a federal controversy.

Id. at 89 (citations and internal quotations omitted). The various formulas the Court has used to describe an insufficient claim—"so attenuated and unsubstantial as to be absolutely devoid of merit," "wholly insubstantial," "obviously frivolous," "no longer open to discussion," or "essentially fictitious," *Hagans v. Lavine*, 415 U.S. 528, 536-37 (1974) (citations omitted)—make clear how minimal the pleading burden is. *See also Traver v. Meshriy*, 627 F.2d 934, 939 (9th Cir. 1980) (Kennedy, J.) (jurisdiction exists even where claim is "tenuous" so long as it is not "frivolous"); 13B Charles Alan Wright, Arthur R. Miller & Edward H. Cooper, Federal Practice and Procedure § 3564, at 70-71 (2d ed. 1984) ("The test for dismissal is a rigorous one and if there is *any* foundation of plausibility to the claim federal jurisdiction exists.") (emphasis added).[30]

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[30] At least since *Douglas v. Wallace*, 161 U.S. 346 (1896), the courts of appeals have uniformly applied this standard. *See, e.g., Cement Masons Health & Welfare Trust Fund for N. California v. Stone*, 197 F.3d 1003, 1008 (9th Cir. 1999) (jurisdiction where claim is "non-

As pled (and proved), UIH's claim was plainly not "frivolous." The Tenth Circuit correctly concluded that UIH "state[d] an actionable 10b-5 claim" under this Court's precedents as well as decisions from the Tenth Circuit and other courts of appeals. *See* Pet. App. B-15. All of Wharf's defenses at trial—that it did not sell UIH the Option, that the Option was subject to unsatisfied conditions, and that the Option was unenforceable under the statute of frauds because UIH's performance was not "fairly referable" to it—were fact-bound. Wharf itself asserts that its statute of frauds defense "required the jury to make [certain] factual determinations." Br. 38; *see also id.* at 18 n.6.

Nor was UIH's claim "foreclosed by prior decisions of this Court" (Br. 41). UIH pled (and proved) a fraudulent "actual sale" of a security. *See supra* pp. 4-5, 10-13. Wharf seeks to extend *Blue Chip* to bar recovery for a sale that depends (in part) on oral testimony. But even if this Court were to agree, its decision would not "foreclose" UIH's claim so as to erase the district court's jurisdiction. That occurs only when the "the *previous* decisions . . . leave no room for the inference that the questions sought to be raised can be the subject of controversy." *Hagans*, 415 U.S. at 538 (emphasis added). As the Court said in *Bell v. Hood*, 327 U.S. 678, 685 (1946), a claim is sufficient to confer jurisdiction if "the right of the petitioners to recover under their complaint will be sustained if the . . . laws of the United States are given one

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frivolous" even if legally insufficient); *EEOC v. St. Francis Xavier Parochial Sch.*, 117 F.3d 621, 623-24 (D.C. Cir. 1997) (jurisdiction because federal claim not "wholly insubstantial and frivolous") (internal quotations omitted); *Plott v. Griffiths*, 938 F.2d 164, 167 (10th Cir. 1991); *Grinter v. Petroleum Operation Support Serv., Inc.*, 846 F.2d 1006, 1008 (5th Cir. 1988); *Traver*, 627 F.2d at 939; *Strachman v. Palmer*, 177 F.2d 427, 429 (1st Cir. 1949) (jurisdiction where claim is not "'so unsubstantial as to be frivolous, or, in other words, . . . plainly without color or merit'" (quoting *Binderup v. Pathe Exchange*, 263 U.S. 291, 305 (1923)). Wharf's suggestion (Br. 40) that "confusion currently prevail[s] in the lower courts" as to the jurisdictional standard is wrong.

construction and will be defeated if they are given another." Both of Wharf's Questions Presented pose—at best—litigable issues: Wharf's "financial information" argument (Question I) has been rejected by several Circuits, *see supra* pp. 36-39 & n.24, and its "enforceability" argument (Question II) concededly turns on questions of fact.[31]

Wharf (Br. 40-41) boldfaces the word "standing" in quotations from several cases in an apparent attempt to suggest that its *Blue Chip* argument, if successful, would eliminate the district court's jurisdiction. But the Court used the word "standing" in each of these cases to refer to a particular plaintiff's lack of a cause of action under a particular statute. "Standing" in that sense is not jurisdictional.[32] *Blue Chip*, for example, did not suggest that because the plaintiff, a nonpurchaser, was ultimately held not to have "standing" to sue under Rule 10b-5, the district court had not had jurisdiction. *See, e.g., Kauthar SDN BHD v.*

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[31] Wharf cannot suggest that UIH's Rule 10b-5 claim was a pretext, "made solely for the purpose of obtaining jurisdiction," *Steel Co.*, 523 U.S. at 89, that UIH never intended to litigate. *Cf. The Fair v. Kohler Die & Specialty Co.*, 228 U.S. 22, 25 (1913) (no jurisdiction where plaintiff is "not really relying upon" the federal law "for his alleged rights"); *Lewis v. United States*, 70 F.3d 597, 603 (Fed. Cir. 1995) (claim insubstantial where "the asserted basis for jurisdiction is . . . pretextual"). UIH actively litigated and won the Rule 10b-5 claim. UIH had reason to bring it: Although the state-law claims arose out of a "common nucleus of operative fact," they required proof of additional legal and factual elements. *Compare* J.A. EM-64-65 (jury instructions on elements of a Rule 10b-5 claim) *with* J.A. EM-25-26 (instructions on elements of fraud).

[32] The Court has discussed the difference between constitutional standing and statutory or prudential standing in a number of cases. *See, e.g., National Credit Union Admin. v. First Nat'l Bank & Trust Co.*, 522 U.S. 479, 488 (1998). Where a statute confers jurisdiction only over cases brought by certain kinds of plaintiffs, the court lacks statutory jurisdiction over a case brought by a nonqualifying plaintiff. *See, e.g., Sierra Club v. Morton* 405 U.S. 727 (1972). But that is not the issue here.

Sternberg, 149 F.3d 659, 663 n.4, 669 n.13 (7th Cir. 1998) (*Blue Chip* standing question is prudential and does not affect court's jurisdiction). Nor was there any suggestion of lack of jurisdiction in *Piper v. Chris-Craft Indus., Inc.*, 430 U.S. 1 (1977), cited by Wharf, which held that tender offerors lack "standing" to sue under Rule 10b-6. *See id.* at 45. None of Wharf's "standing" cases was dismissed for lack of jurisdiction. The "question whether a federal statute creates a claim for relief is not jurisdictional." *Northwest Airlines, Inc. v. County of Kent, Michigan*, 510 U.S. 355, 365 (1994).[33]

The district court's decision to exercise jurisdiction over the supplemental state law claims under § 1367 was likewise proper. Wharf does not dispute that these claims were "so related to claims in the action within . . . original jurisdiction [*i.e.*, the Rule 10b-5 claim] that they form part of the same case or controversy." 28 U.S.C. § 1367(a). The specific elements of proof for these claims were different, but all of them "derive from a common nucleus of operative fact." *United Mine Workers v. Gibbs*, 383 U.S. 715, 725 (1966).[34] Although Wharf adverts (Br. 44) to two of the grounds (allegedly predominant state claims and novel state law issues) on which a district court "may," if it chooses, decline jurisdiction, *see* 28 U.S.C. § 1367(c), Wharf does not claim

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[33] *See Powers v. British Vita, P.L.C.*, 57 F.3d 176, 188 (2d Cir. 1995) (affirming dismissal on the merits); *Jacobson v. AEG Capital Corp.*, 50 F.3d 1493 (9th Cir. 1995) (affirming dismissal under Fed. R. Civ. P. 12(b)(6), not 12(b)(1)). In one of Wharf's cases, the court declined to address the "standing" argument because it "was not presented in . . . the court below"; the court's explanation makes clear that the court did not use "standing" in a jurisdictional sense. *See 7547 Corp. v. Parker & Parsley Dev. Partners, L.P.*, 38 F.3d 211, 229 (5th Cir. 1994).

[34] *See, e.g.*, *McGrath*, 651 F.2d at 464 (where complaint sets forth non-frivolous Rule 10b-5 claim, court has pendent jurisdiction over state law fraud and breach of contract claims; "The defendants' asserted liability, under both federal and state law, rests on the same set of events, and proof would require largely the same evidence.")

that the district court's original decision to accept jurisdiction was an abuse of discretion. Further, Wharf's suggestion that these state law questions are novel is both a new argument and wrong. The Tenth Circuit, citing ample Colorado precedent, rejected Wharf's arguments based on existing Colorado case law. *See supra* pp. 18, 40-42.

C. Even if This Court Were Now To Reject UIH's Rule 10b-5 Claim on the Merits, There Would Be No Reason To Overturn the Judgment on the State-Law Claims After Six Years of Litigation.

Wharf's brief seeks to muddle the well established rules for dealing with supplemental state-law claims when a federal claim is rejected. If the federal claim is so insubstantial that the district court lacks subject matter jurisdiction, then dismissal of all claims is of course mandatory, regardless of when in the litigation this is determined. But where the federal claim is not frivolous, and is dismissed on its merits, the district court has *discretion* whether to retain the supplemental claims. *See* 28 U.S.C. § 1367(c) ("The district court *may* decline to exercise supplemental jurisdiction over a claim . . . if . . . the district court has dismissed all claims over which it has original jurisdiction.") (emphasis added).

If there is jurisdiction, the question whether to retain the supplemental claims turns on "considerations of judicial economy, convenience and fairness to litigants," taking into account "the already completed course of the litigation." *Gibbs*, 383 U.S. at 726, 727. Where the federal claim is not rejected until after a full trial, the law is as clear and consistent as it is sensible: "Once a trial is held . . . [a] court will order dismissal of a pendent claim on remand only when the federal cause of action was so insubstantial and devoid of merit that there was no federal jurisdiction to hear it." *Traver*, 627 F.2d at 939 (Kennedy, J.); Pet. App. B-13 (adopting the same formulation as *Traver*). As the Seventh

Circuit explained in *Graf v. Elgin, Joliet and E. Ry. Co.*, 790 F.2d 1341, 1347-48 (7th Cir. 1986):

> Judicial economy . . . supports the retention of pendent jurisdiction in any case where substantial judicial resources have already been committed, so that sending the case to another court will cause a substantial duplication of effort. Trial is simply a convenient benchmark marking the point by which substantial resources have surely been committed.

(citations omitted). Federal courts consistently retain the state law claims in these circumstances, to avoid the waste and gross unfairness that would result from nullification of completed proceedings.[35]

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[35] *See, e.g., Textile Deliveries, Inc. v. Stagno*, 52 F.3d 46, 48-49 (2d Cir. 1995) (after dismissing federal claim at close of plaintiff's case, state law claims properly sent to jury); *Gilbert/Robinson, Inc. v. Carrie Beverage-Missouri, Inc.*, 989 F.2d 985, 993 (8th Cir. 1993) (where federal claim found meritless after first part of bifurcated trial, proper to proceed with rest of trial on state law causes of action only); *Transcontinental Leasing, Inc. v. Michigan Nat'l Bank of Detroit*, 738 F.2d 163, 165-66 (6th Cir. 1984); *Caserta v. Village of Dickinson*, 672 F.2d 431, 433 (5th Cir. 1982) ("[c]ourt should be reluctant to dismiss a pendent claim once substantial time and resources have been devoted to such claims[.]"); *Parrent v. Midwest Rug Mills, Inc.*, 455 F.2d 123, 129 (7th Cir. 1972), *overruled on unrelated grounds by Short v. Belleville Shoe Mfg. Co.*, 908 F.2d 1385 (7th Cir. 1990) (review of state law claims on the merits after dismissing the federal claims on appeal); *Forest Labs., Inc. v. Pillsbury Co.*, 452 F.2d 621, 629 (7th Cir. 1971) ("'Considerations of judicial economy, convenience and fairness to litigants' certainly favor the retention of jurisdiction over state law issues, where both state and federal claims were tried together and the latter only dismissed after trial.") (citation omitted); *A. H. Emery Co. v. Marcan Prods. Corp.*, 389 F.2d 11, 19-21 (2d Cir. 1968) (adjudication of state law claim after dismissal of federal claim at end of plaintiff's case); *see also* 16 James W. Moore et al., Moore's Federal Practice § 106.66[3][a], at 106-90 (3d ed. 1999) ("One reason that a federal court will retain jurisdiction over a supplemental claim after dismissal of all jurisdiction-conferring claims is if substantial judicial resources have already been committed, resulting in

None of Wharf's cases is to the contrary. Two of them involve dismissals for lack of jurisdiction and are wholly irrelevant. *See Wellness Cmty. (R)-Nat'l v. Wellness House*, 70 F.3d 46, 49-50 (7th Cir. 1995) (diversity case; amount in controversy insufficient); *Gaff v. FDIC*, 814 F.2d 311, 318-19 (6th Cir. 1987) (federal claim as pled too insubstantial to confer jurisdiction). And in each of Wharf's cases, the federal claim was dismissed or abandoned before any trial of the pendent claims. *See Seabrook v. Jacobson*, 153 F.3d 70, 71 (2d Cir. 1998) (federal claim dismissed before trial; important state issues truly of first impression); *Doe v. Sundquist*, 106 F.3d 702, 707 (6th Cir. 1997) (appeal from denial of preliminary injunction; plaintiffs' chance of success on the federal claims "so slim as to be entirely ephemeral"); *Wellness Cmty.*, 70 F.3d at 50 ("federal claim was abandoned by the plaintiff before the trial ever started"); *Gaff*, 814 F.2d at 314-15 (federal claim dismissed before trial); *Tully*, 540 F.2d at 189, 196-97 (federal question resolved against plaintiffs on the papers "without trial"; no prejudice to plaintiffs because parallel state case pending).[36] Wharf suggests (Br. 40) that lower courts are "confus[ed]" and apply different standards to the dismissal of pendent claims, but it is Wharf that is confusing the rules. No case any party has found remotely suggests that a jury verdict on state law claims should be jettisoned merely because a federal claim that created jurisdiction is rejected on appeal.

In this case, considerations of "judicial economy, convenience and fairness" would overwhelmingly favor retaining the state-law verdicts. The case comes to this Court

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a substantial duplication of effort if the matter is now to be adjudicated in another court.").

[36] Wharf particularly stresses *Tully*, but the Third Circuit's post-*Tully* decision in *Lentino v. Fringe Employee Plans, Inc.*, 611 F.2d 474, 479-80 (3d Cir. 1979), wholly undermines Wharf's argument. *See id.* (upholding exercise of pendent jurisdiction where federal claim dropped on morning of trial).

after two years of discovery; an eleven-week jury trial involving thirty-nine witnesses from the United States, Europe, and Asia; two interlocutory appeals; and two complex appeals after the judgment. The wastefulness of repeating the massive expenditure of resources is obvious, as is the inconvenience to all concerned of starting over six years later in a Colorado court. And there is no reason at all for the manifest unfairness of giving Wharf a "second bite."

No considerations point the other way. Wharf's only argument, based on "comity" (Br. 44, 45) is frivolous. Wharf never claimed below that a federal court could not resolve the two state-law questions (concerning former Colo. Rev. Stat. § 4-8-319 and Colorado's application of the "economic loss rule") and never asked the lower courts to certify any question to the state courts.[37] As noted above, the Tenth

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[37] Wharf's claim (Br. 45 n.9) that there is "great unsettlement" in Colorado law, making certification appropriate, also comes too late. As the very case Wharf cites makes clear, this Court "do[es] not suggest that where there is doubt as to local law and where the certification procedure is available, resort to it is obligatory." *Lehman Bros. v. Schein*, 416 U.S. 386, 390-91 (1974). "If a district court or court of appeals believes that it can resolve an issue of state law with available research materials already at hand, and makes the effort to do so, its determination should not be disturbed simply because the certification procedure existed but was not used." *Id.* at 395 (Rehnquist, J., concurring). Except in exceptional circumstances not presented here, appellate courts will not certify a question to the state courts where the party failed to seek certification below. *See Stenberg v. Carhart*, 530 U.S. 914, 120 S. Ct. 2597, 2617 (2000); *Emerito Estrada Rivera-Isuzu de P.R., Inc. v. Consumers Union of United States, Inc.*, 233 F.3d 24, 29-30 (1st Cir. 2000); *Boyd Rosene & Assocs. v. Kansas Mun. Gas Agency*, 178 F.3d 1363, 1364 (10th Cir. 1999) ("Late requests . . . rarely granted . . . and are generally disapproved, particularly when the district court has already ruled."); *In re McLinn*, 744 F.2d 677, 681 (9th Cir. 1984) ("particularly compelling reasons must be shown" and requests are ordinarily rejected when "the district court employed a reasonable interpretation of state law"); *see also* 17A Wright, Miller & Cooper, *supra*, § 4248 (Supp. 2000) ("[F]ailure of a party to suggest certification until a late stage in the proceeding considerably weakens his insistence on certification.").

Circuit carefully applied clear Colorado precedents to answer each question, and Wharf's supposedly conflicting cases arose under the laws of other States. *See supra* p. 40 & n.27.

CONCLUSION

The judgment of the United States Court of Appeals for the Tenth Circuit should be affirmed.

Respectfully submitted,

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